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IN THE

Supreme Court of the United States

OCTOBER TERM, 1931.

No. 634.

THE TEXAS & PACIFIC RAILWAY COMPANY,
Petitioner,

vs.

UNITED STATES.

BRIEF FOR PETITIONER ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

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INDEX.

	PAGE
OPINION OF THE COURT BELOW	1
JURISDICTION	1
STATEMENT OF THE CASE	2
STATUTES INVOLVED	3
QUESTION INVOLVED	3
SPECIFICATION OF ERRORS	3
SUMMARY OF ARGUMENT	4
ARGUMENT	5
PRELIMINARY STATEMENT	5
I. THE "GUARANTY" PAYMENT UNDER THE TRANSPORTATION ACT, 1920, WAS A GOVERNMENT SUBSIDY DESIGNED TO INSURE AN ADEQUATE TRANSPORTATION SYSTEM FOR THE COUNTRY	6
1. The situation of the railroads at the end of Federal control and the purpose of the Transportation Act, 1920	6
2. There was no legal obligation on the Government to make the "guaranty"	8
3. The "guaranty" payment was not income from operation of the railroads but was a subsidy	9
II. BEING A SUBSIDY, the "GUARANTY" PAYMENT IS NOT "INCOME" WITHIN THE MEANING OF THE SIXTEENTH AMENDMENT	11

PAGE

1. A subsidy is not taxable as "income" 11

2. Mutuality and consideration for the agreement to pay the "guaranty" does not make the payment taxable as "income" 12

3. The way in which the "guaranty" payment might be spent does not determine its status as "income" 14

4. Income Defined 15

CONCLUSION 16

APPENDIX:

Excerpts from Revenue Act of 1918, Sections 213, 233.. 17
Excerpts from Transportation Act, 1920, Section 209.. 18

Table of Cases.

PAGE

Birmingham Trust & Savings Co. v. Atlanta, etc., Ry. Co., 300 Fed. 173 ..... 4, 9
Blodgett v. Holden, 275 U. S. 142 ..... 13, 16
Bowers v. Kerbaugh-Empire Co., 271 U. S. 170 ..... 4, 13
Eastern Extension, etc. Tel. Co. Ltd. v. United States, 251 U. S. 355 8
Edwards v. Cuba Railroad Co., 268 U. S. 628 ..... 4, 11-12, 13
Eisner v. Macomber, 252 U. S. 189 ..... 5, 13, 15, 16
Flint v. Stone Tracy Co., 220 U. S. 107 9
Merchants' Loan & Trust Co., Trustee v. Smietanka, 255 U. S. 509 15
Miles v. Safe Deposit Co., 259 U. S. 247 13
Smietanka v. First Trust & Savings Bank, 257 U. S. 602. 16
Stratton's Independence Ltd. v. Howbert, 231 U. S. 399. 9
United States v. Guaranty Trust Co., 280 U. S. 478 ..... 4, 6, 14
United States v. Merriam, 263 U. S. 179 ..... 5, 13, 14
United States v. Supplee-Biddle Hardware Co., 265 U. S. 189 ..... 4, 13

Statutes Cited.

Act of Congress of February 13, 1925 1
Corporation Excise Tax Act of August 5, 1909 9
Federal Control Act 2, 3, 5, 8
Revenue Act of 1918 ..... 2, 3, 17
Revenue Act of 1918, Sections 213 and 233 (Appendix). 17
Transportation Act, 1920 ..... 2, 3, 4, 5, 6, 8, 10, 13, 16, 18
Transportation Act, 1920, Section 209 (Appendix) 18-22

Miscellaneous Citations.

Congressional Record, Vol. 58, Part 8 ..... 7, 8
Congressional Record, Vol. 58, Part 9 ..... 10, 11
Congressional Record, Vol. 59, Part 4 ..... 7, 10
Finance Docket No. 1176, 70 I. C. C. 115 8

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BRIEF FOR PETITIONER ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

On writ of certiorari to the United States Court of Claims to review a judgment in an action for the refund of Federal income and excess profits taxes.

Opinion of the Court Below.

The opinion of the Court of Claims is reported in 52 Fed. (2d) 1040 (R. 13).

Jurisdiction.

The jurisdiction of the Court is invoked under Section 3(b) of the Act of Cong. February 13, 1925, c. 229, 43 Stat. 936, 939, amending Section 240 of the Judicial Code.

A petition for a writ of certiorari was filed on January 14, 1932 (R. 18) and was granted February 15, 1932 (R. 19).

Statement of the Case.

This is a suit to recover $208,138.01, part of the income and excess profits taxes paid by Petitioner for the year 1920 under the provisions of the Revenue Act of 1918 (Act of Cong. Feb. 24, 1919, c. 18), 40 Stat. 1057 (R. 8).

Petitioner is a railroad corporation and during the months of January and February, 1920, its properties were operated by the Director General of Railroads under the Federal Control Act (Act of Cong. Mar. 21, 1918, c. 25), 40 Stat. 451 (R. 9).

Federal Control terminated on February 29, 1920, under the provisions of the Transportation Act, 1920 (Act of Cong. Feb. 28, 1920, c. 91), 41 Stat. 456, and, during the remainder of the calendar year 1920, the Petitioner was operated by a receiver under a decree of court (R. 9).

Petitioner accepted the provisions of Section 209 of the Transportation Act, 1920, and under the "guaranty" received for the period of six months after Federal Control ceased, called the "guaranty period", the sum of $2,043,041.77, and one of its two subsidiaries received $18,040.86, a total of $2,061,082.63 (R. 9).

For the year 1920 Petitioner filed its tax return and reported thereon and paid a tax of $332,976.71 (R. 9). Petitioner's two subsidiaries filed separate tax returns and reported losses (R. 10).

The Commissioner of Internal Revenue upon audit and reaudits of the 1920 returns in 1925, 1926 and 1927, consolidated the Petitioner and its subsidiaries (R. 10-11), made various adjustments to income and finally, in April 1927, determined a consolidated net income of $3,639,968.48 (R. 11), and a tax liability of Petitioner and its subsidiaries of $363,796.85, which was allocated $361,797.42 to the Petitioner and $1,999.43 to one of its subsidiaries (R. 12). The resulting deficiency in tax of the Petitioner of $28,820.71 was duly paid (R. 12). The total net tax paid by Petitioner after reimbursement made by the Director General of Railroads was $349,737.51 (R. 12).

The Commissioner of Internal Revenue in determining the consolidated net income of Petitioner and its subsidiaries for the year 1920 included as income the "guaranty" payment of $2,061,082.63 made under Section 209(c)(1) of the Transportation Act, 1920 (R. 12).

Thereafter the Petitioner duly filed a claim for refund of $206,108.26 based upon the erroneous inclusion in income of the "guaranty" payment and a claim for $2,029.75 based upon certain minor items (R. 12).

The Commissioner of Internal Revenue rejected the claims for refund (R. 12) and this suit was brought within two years from the date of rejection (R. 3).

The Court of Claims gave judgment for the Petitioner for $1,962.09 (R. 13), sustaining the Petitioner's contentions as to the minor items. The Court held, however, that the "guaranty" payment of $2,061,082.63 was "income" subject to tax (R. 15).

Statutes Involved.

The Statutes involved are the Revenue Act of 1918 (Act of Cong. February 24, 1919, c. 18), 40 Stat. 1057, and Section 209(c)(1) of the Transportation Act, 1920 (Act of Cong. Feb. 28, 1920, c. 91), 41 Stat. 456, 464-467. Pertinent excerpts from these Acts are set out in the Appendix hereto.

Question Involved.

Was the "guaranty" payment under Section 209(c)(1) of the Transportation Act, 1920, a "subsidy" or taxable as "income" under the Revenue Act of 1918 and the Sixteenth Amendment to the Constitution?

Specification of Errors.

1. The Court of Claims erred in holding that the "guaranty" payment to Petitioner under Section 209 of the Transportation Act, 1920, was "income" taxable under the Revenue Act of 1918 and the Sixteenth Amendment to the Constitution.

2. The Court of Claims erred in not entering judgment for Petitioner in the sum of $201,200.07, the amount of taxes overpaid for 1920 on excluding the "guaranty" payment from "income".

Summary of Argument.

I. The condition of the railroads at the termination of Federal control was such that rehabilitation was necessary to insure an adequate transportation system. The purpose of the Transportation Act, 1920, was to remedy this situation. *United States* v. *Guaranty Trust Co.*, 280 U. S. 478.

Congress recognized the immediate need of the railroads for additional "capital". Without any legal obligation on the part of the Government, the Transportation Act was passed providing for a "guaranty" payment.

The "guaranty" payment was not income from operation of the railroad. *Birmingham Trust & Savings Co.* v. *Atlanta etc. Ry. Co.*, 300 Fed. 173. The payment was in fact and was intended by Congress as a subsidy.

II. Being a subsidy the "guaranty" payment is not income within the meaning of the Sixteenth Amendment. *Edwards* v. *Cuba Railroad Co.*, 268 U. S. 628. Every economic advantage or receipt of money does not result in "income". Mutuality and consideration did not remove the "guaranty" payment from the category of a subsidy or convert it into "income". *Edwards* v. *Cuba Railroad Co., supra; United States* v. *Supplee-Biddle Hardware Co.*, 265 U. S. 189; *Bowers* v. *Kerbaugh-Empire Co.*, 271 U. S. 170. The provision for payment by the railroads to the Government of any excess over the "guaranty" was a limitation or condition to eliminate carriers not in need of the subsidy. It was not inserted as a money producing provision for the Government. It was designed primarily as an administrative measure to eliminate applications by carriers not in need of financial assistance and to save auditing expenses and delay.

The nature of the "guaranty" payment, and not the manner in which it might be spent, determines whether it is "income". *United States* v. *Merriam*, 263 U. S. 179. The "guaranty" payment was not derived from capital or labor, or from both combined. It was not "income" within the definition which this Court has adopted and consistently followed, *Eisner* v. *Macomber*, 252 U. S. 189, as a limitation upon the power of Congress under the Sixteenth Amendment.

ARGUMENT.

Preliminary Statement.

The question of the taxability as "income" of the payment under Section 209(c)(1) of the Transportation Act, 1920, is not to be confused with payments made to carriers under the Federal Control Act as compensation for the use by the Government of railroad properties during Federal Control. The Transportation Act terminated Federal Control on February 29, 1920.

Payments under the Federal Control Act are admittedly "income" and subject to tax. Taxes based on those payments and on earnings of Petitioner from operation of its road in 1920 are *not* sought to be recovered in this action.

This case involves a "guaranty" payment under the Transportation Act, 1920, for the period of six months, March 1, 1920, to August 31, 1920, called "the guaranty period", after possession and use by the Government had ended and the properties had been returned to private ownership.

Section 209 provides for a "guaranty" payment by the Government under various conditions prescribed therein. This case falls under Section 209(c)(1) as the Petitioner had a contract fixing just compensation for the Federal Control period. In this case the amount of the "guaranty" payment is the excess of one-half of the annual amount fixed as "just compensation" in the Federal Control contract over "railway operating income."

"Railway operating income" (a term defined by the Interstate Commerce Commission in its Regulations, "Issue of 1914", governing the "Classification of Income, Profit and Loss for Steam Roads") is an amount determined by deducting from "railway operating revenues", the items of "railway operating expenses", "railway tax accruals", and "uncollectible railway revenues."

I.

The "Guaranty" Payment Under the Transportation Act, 1920, Was a Government Subsidy Designed to Insure An Adequate Transportation System for the Country.

1. The situation of the railroads at the end of Federal control and the purpose of the Transportation Act, 1920.

Government operation of railroads during the war years had resulted in a critical situation and the maintenance of a transportation system for the United States was at stake. Tracks, structures and rolling stock had deteriorated. Additions and betterments were imperative. Funds were needed for improvements, expansion and additional equipment. The railroads had to be rehabilitated from the standpoint of "capital."

The condition of the railroads when the Transportation Act, 1920, was passed and the purpose to preserve for the nation the whole existing transportation system was stated by this Court in *United States* v. *Guaranty Trust Co.*, 280 U. S. 478, as follows:

> "These appropriations were made in order to meet a pressing need. At the time of the passage of Transportation Act, 1920, most of the railroads of the United States lacked funds for necessary improvements, equipment, and expansion of facilities. Some of the carriers needed funds, also, to meet maturing obligations. The credit of

> many carriers was seriously impaired. There was a general reluctance among investors to purchase new railroad securities even of the strongest railroads. Congress deemed it important to preserve for the nation substantially the whole existing transportation system. Compare *New England Divisions Case*, 261 U. S. 184, 190". (p. 484).

The same purpose was expressed by Congress.

Senator Cummins, Chairman of the Interstate Commerce Committee of the Senate, said (Cong. Rec., Vol. 59, Part 4, p. 3327):

> "Without entering into the details of the situation it is well known to every observer that we need from 100,000 to 200,000 additional cars, we need more main tracks, more side tracks, more warehouses, and more terminal facilities of all kinds. If the railways are to succeed in giving to the people what they must have, if we are to prosper, these companies must borrow or secure in some way not less than $600,000,000 this year and $1,000,000,000 next year."

Representative Cooper, a member of the Interstate Commerce Committee of the House, said (Cong. Rec., Vol. 59, Part 4, p. 3308):

> "* * * It is estimated that about 200,000 new cars must be built in 1920 to make good the deficiency.
>
> It is also stated that the normal railroad requirements are about 3,000 new locomotives per year, yet during Federal control only 2,000 locomotives, or one-third of the normal requirement has been provided. Only 923 new passenger cars have been purchased in over two years and only 721 miles of railroad extension have been built."

Representative Barkley, a member of the Interstate Commerce Committee of the House, said (Cong. Rec., Vol. 58, Part 8, p. 8445):

> "Therefore as a matter of fact if we do not help them to finance at this time these capital investments they

> will have to go into the markets at the present high rate of money and finance them themselves. And the inability to do so is going to put many of the railroads into the hands of receivers."

Representative Barkley (Cong. Rec., Vol. 58, Part 8, p. 8331):

> "I think it is not going too far to say that if we on the 31st of December were to turn the roads back to their owners without remedial legislation, it would result in the most disastrous financial panic that the country has ever seen."

2. There was no legal obligation on the Government to make the "guaranty".

The "guaranty" payment to Petitioner did not arise from any legal obligation on the part of the Government.

See: *Finance Docket No. 1176,* 70 I. C. C. 115, 116.

Compares: *Eastern Extension, etc. Tel. Co. Ltd.* v. *United States,* 251 U. S. 355, 363-364.

The Federal Control Act provided for the settlement of all matters growing out of the Federal control period. The Transportation Act did not apply to that period or to settlements based on use of the properties by the Government during Federal Control.

Furthermore, it should be noted that Section 209, by Subdivision (c)(4), makes the Act equally applicable to carriers that had not been under Federal control.

The Court of Claims in its opinion admits that there was "no legal obligation in enacting this legislation requiring the Government to make these payments," but says "that there were obligations of 'an equitable, moral, and honorary nature'" which "may well be said to take the place of a legal obligation."

3. The "guaranty" payment was not income from operation of the railroads but was a subsidy.

The "guaranty" payment was not derived from services rendered or to be rendered by the Petitioner to the United States. It was not compensation for use of the railroad properties by the Government which ended March 1, 1920. It was not a profit or gain derived from the use or operation of the railroad by the Petitioner.

> "The guaranty money was not produced by railroad operation."
>
> *Birmingham Trust and Savings Co.* v. *Atlanta, etc., Ry. Co.*, 300 Fed. 173, 179.

Petitioner's earnings from operation of its railroad in 1920 have been included in taxable income and the tax paid thereon is not contested in this suit.

While "railway operating income" on the one hand, and one-half of the annual amount of "just compensation" specified in the Federal Control contract on the other hand, are used in this case as the basis for computing the amount of the "guaranty" payment, the subsidy itself is the result of comparing those factors.

The "guaranty" payment is neither "railway operating income" nor "just compensation" as those terms are used only as a measure to determine, first, qualification for receiving the subsidy, and, second, the amount of the subsidy. Used as a yardstick or measure they do not characterize the "guaranty" payment as either "operating income" or "just compensation". The terms are used in the same capacity as "income" was used as a measure for the Corporation Excise Tax levied by the Act of August 5, 1909, c. 6, 36 Stat. 113. Although income was there used as the measure, this Court held that the Act levied an "Excise" and not an "income" tax.

> *Flint* v. *Stone Tracy Co.*, 220 U. S. 107;
> *Stratton's Independence Ltd.* v. *Howbert*, 231 U. S. 399.

While section 209(d) provides that any excess of "railway operating income" over one-half the amount named in the Federal Control contract must be paid into the Treasury there was no excess in this case.

To say that "operating income" was guaranteed is not only erroneous but begs the question of the fundamental nature of the payment. Was it "income" or a "subsidy" as intended by Congress?

The particular language used in section 209 of the Transportation Act, 1920, is of importance. It states "The United States hereby guarantees", it provides a "guaranty" and refers to "the guaranty period".

Payments under Section 209 of the Transportation Act, 1920 were referred to by members of Congress as a "subsidy" or "gift".

As typical we quote Representative Kitchen (Cong. Rec., Vol. 59, Part 4, p. 3313):

> "In my judgment, and I make the prediction that it will require practically the entire amount of the standard return for the six months, that is, $475,000,000, to make good the guaranty.
>
> Whatever the amount shall be, it is an absolute gift by the Government to the railroads—the deliberate taking out of the pockets of the taxpayers and giving it to the railroad owners."

Representative Sims, a member of the Interstate Commerce Committee of the House (Cong. Rec., Vol. 59, Part 4, p. 3289):

> "But not satisfied with this burden upon the people, we give a subsidy for the first six months."

Representative Steagall (Cong. Rec., Vol. 58, Part 9, p. 8675):

> "They (the people) are going to be sorely disappointed when they learn that this bill looks to an increase of these burdens along with its enormous subsidy to the roads."

Representative Box (Cong. Rec., Vol. 58, Part 9, p. 9189):

> "The amount which this will cost the Government, in guaranties and subsidies, will run into hundreds of millions, which, in addition to the sums loaned to the roads, will be taken from the public treasury at a time when the Government is already paying out from one to four billion dollars more per year than it is receiving in taxes and revenues, and will greatly increase the already heavy deficits."

The "guaranty" payment was not received for services rendered to the United States. The payment was not derived from capital. It was a Government subsidy or aid, so intended by Congress, with the view of protecting and insuring an efficient system of transportation for the people.

II.

Being a Subsidy, the "Guaranty" Payment Is Not "Income" Within the Meaning of the Sixteenth Amendment.

1. A Subsidy Is Not Taxable as "Income".

This case is controlled by the decision of this Court in *Edwards* v. *Cuba R. R. Co.*, 268 U. S. 628, holding that subsidies paid to a railroad by the Cuban Government were not taxable as "income" under the Sixteenth Amendment to the Constitution. In that case the Cuban Government granted subsidies to a New Jersey railroad corporation based on the number of miles of line constructed. To receive the subsidies the railroad company had to comply with certain definite requirements, and by executed contracts the company agreed to a one-third reduction in rates for transportation of employees and troops of the Government, to reduce first class rates, to carry public correspondence free, to carry small produce for one-half the tariff, to allow the Government to

establish telegraph and telephone stations along the railroad and to transport troops in special trains at special rates in case of war.

Under these circumstances, this Court said:

> • • • "The Cuban laws and contracts are similar to legislation and arrangements for the promotion of railroad construction which have been well known in the United States for more than half a century. Such aids, gifts and grants from the government, subordinate political subdivisions or private sources,—whether of land, other property, credit or money,—in order to induce construction and operation of railroads for the service of the public are not given as mere gratuities. *Burke* v. *Southern Pacific R. R. Co.*, 234 U. S. 669, 679; *Louisville & Nashville R. R.* v. *United States*, 267 U. S. 395. Usually they are given to promote settlement and to provide for the development of the resources in the territory to be served. The things so sought to be attained in the public interest are numerous and varied. • • • The subsidy payments were proportionate to mileage completed; and this indicates a purpose to reimburse plaintiff for capital expenditures. • • • The subsidy payments taxed were not made for services rendered or to be rendered. They were not profits or gains from the use or operation of the railroad, and do not constitute income within the meaning of the Sixteenth Amendment. See *Stratton's Independence* v. *Howbert*, 231 U. S. 399, 415; *Eisner* v. *Macomber*, 252 U. S. 189, 207; *Merchants' Loan & Trust Co.* v. *Smietanka, supra.*" (pp. 632-633).

2. Mutuality and consideration for the agreement to pay the "guaranty" does not make the payment taxable as "income".

In this respect the instant case is even stronger than the *Cuba Railroad Case* (*supra*). In the *Cuba Case* the company agreed, by executed contracts, to reduce existing rates one-third for carrying Government troops and employees, to carry Government mails free, to reduce rates for first-class passengers, to carry small produce for one-half the tariff, to allow the Government to establish telegraph and tele-

phone stations along the railroad and in case of war to transport troops in special trains at special rates.

All these were conditions attached to receiving the subsidy and were considerations for its payment. There was real consideration and mutuality of obligation. Even under these conditions this Court held that the considerations and the mutual and contractual obligations of the railroad and the Government did not render the payments "income".

Every valid contract must rest upon consideration, but consideration as such does not necessarily make the amount received under the contract "income" within the definition of this Court. Consideration for a contract cannot alone create "income". Every economic advantage or receipt of money does not result in "income". This Court has so held in the case of proceeds of insurance on the life of an officer (*United States* v. *Supplee-Biddle Hardware Co.*, 265 U. S. 189), the extinguishment of a debt for less than its face (*Bowers* v. *Kerbaugh-Empire Co.*, 271 U. S. 170), and a subsidy payment (*Cuba Railroad Case, supra*). In those cases the amounts were received under contracts based upon real consideration and mutuality of obligation.

Also the receipt of a stock dividend (*Eisner* v. *Macomber*, 252 U. S. 189), and a stock right (*Miles* v. *Safe Deposit Co.*, 259 U. S. 247), were held not to be "income". Furthermore, a bequest to an executor in lieu of compensation (*United States* v. *Merriam*, 263 U. S. 179), and a gift (*Blodgett* v. *Holden*, 275 U. S. 142), have been held not to be taxable "income".

That the petitioner assented to the provisions of the Transportation Act and agreed, on the remote condition of excess earnings, to pay such excess to the Government cannot alter or affect the question of whether the subsidy paid was, in fact, "income".

The purpose of Section 209 was to give Governmental aid to those carriers which needed rehabilitation, and thus to insure transportation facilities to the country at large. Such aid to be effective would have to be prompt. With this pur-

pose in mind it was necessary to exclude carriers which were not in need of aid. The provision that a qualifying carrier realizing an excess during the guaranty period must pay such excess into the Treasury was a limitation or condition that effectively eliminated from the subsidy carriers which did not need it. The condition likewise relieved the Interstate Commerce Commission of an enormous auditing and expense burden. The provision as to excess earnings was really a condition limiting payment to only those carriers in need. It would be absurd to consider the condition as a money producing provision. It was recognized from the outset that the Government would receive little or nothing under the provision, but on the other hand would be compelled to pay the subsidies.

3. The way in which the "guaranty" payment might be spent does not determine its status as "income".

The nature or character of the "guaranty" payment cannot be determined from its use. Taxability as "income" does not depend upon how the money received is spent, whether for capital additions, current expenses or what not. If in its nature the "guaranty" is not "income" within the definition of this Court, the use to which it is put cannot convert it into "income".

Compare: *United States* v. *Merriam*, 263 U. S. 179.

While there was no restriction on how the "guaranty" payment was spent, the railroads urgently needed "capital" for cars, tracks, terminal facilities, buildings, capital improvements, additions and betterments and the purpose of the Act was to meet that need.

See: *United States* v. *Guaranty Trust Co.* (*supra*, p. 6);
Statement of Senator Cummins (*supra*, p. 7);
Statement of Representative Cooper (*supra*, p. 7).

4. Income Defined.

This Court in the case of *Eisner* v. *Macomber*, 252 U. S. 189, defined "income", within the meaning of the Sixteenth Amendment to the Constitution, as follows:

> "* * * 'Income may be defined as the gain derived from capital, from labor, or from both combined,' provided it be understood to include profit gained through a sale or conversion of capital assets, to which it was applied in the *Doyle Case* (pp. 183, 185)."
>
> "* * * The Government, although basing its argument upon the definition as quoted, placed chief emphasis upon the word 'gain,' which was extended to include a variety of meanings; while the significance of the next three words was either overlooked or misconceived. *'Derived-from-capital';*—'the *gain-derived-from-capital,*' etc." (p. 207).

In the case of *Merchants' Loan & Trust Co., Trustee* v. *Smietanka*, 255 U. S. 509, the above definition was followed (pp. 517-518) without modification or change, this Court being "entirely satisfied" with the completeness of the definition.

The definition of income in the *Macomber Case* was not casual or used by way of illustration. It represents an all-inclusive rule established for future use in determining what is "income". The Court after defining income then considered whether a stock dividend fell within its terms. This established definition has been consistently used in deciding all subsequent cases involving the question of what is "income".

As to the constitutional limitation upon Congress and the distinction between what is and what is not "income" this Court said in the *Macomber Case*, at page 206:

> "In order, therefore, that the clauses cited from Article I of the Constitution may have proper force and effect, save only as modified by the Amendment, and that the latter also may have proper effect, it becomes essen-

> tial to distinguish between what is and what is not 'income', as the term is there used; and to apply the distinction, as cases arise, according to truth and substance, without regard to form. Congress cannot by any definition it may adopt conclude the matter, since it cannot by legislation alter the Constitution, from which alone it derives its power to legislate, and within whose limitations alone that power can be lawfully exercised."

The constitutional limitation upon the power of Congress to levy taxes must be strictly complied with.

> *Eisner* v. *Macomber*, 252 U. S. 189, 206, 211;
> *Smietanka* v. *First Trust & Savings Bank*, 257 U. S. 602, 605-606;
> *Blodgett* v. *Holden*, 275 U. S. 142, 148.

Congress, under the Sixteenth Amendment, has only the power to tax "income" in fact. If no income is in fact received there is no basis for the tax.

The "guaranty" payment under Section 209 of the Transportation Act, 1920, was not "derived" from "capital or labor" nor from "a sale or conversion of capital assets." It was not "income" under the definition of this Court.

CONCLUSION.

The "guaranty" payment lacks every characteristic necessary to constitute "income" as this Court has defined that term. The Court of Claims was in error in holding that the payment was "income" subject to taxation.

The judgment below should be modified accordingly.

Respectfully submitted,

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APPENDIX.

Revenue Act of 1918.

(40 Stat. 1057)

SECTION 213. (40 Stat. 1065.)

"SEC. 213. That for the purposes of this title (except as otherwise provided in section 233) the term 'gross income'—

(a) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including in the case of the President of the United States, the judges of the Supreme and inferior courts of the United States, and all other officers and employees, whether elected or appointed, of the United States, Alaska, Hawaii, or any political subdivision thereof, or the District of Columbia, the compensation received as such), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period; but

(b) Does not include the following items, which shall be exempt from taxation under this title:

* * * * * * *

(3) The value of property acquired by gift, bequest, devise, or descent (but the income from such property shall be included in gross income);"

SECTION 233. (40 Stat. 1077.)

"SEC. 233. (a) That in the case of a corporation subject to the tax imposed by section 230 the term 'gross income' means the gross income as defined in section 213 * * *" with certain enumerated exceptions which are here immaterial.

Transportation Act of 1920.

SECTION 209. (41 Stat. 456, 464-467.)

GUARANTY TO CARRIERS AFTER TERMINATION OF FEDERAL CONTROL.

"SEC. 209. (a) When used in this section—

The term 'carrier' means (1) a carrier by railroad or partly by railroad and partly by water, whose railroad or system of transportation is under Federal control at the time Federal control terminates, or which has heretofore engaged as a common carrier in general transportation and competed for traffic, or connected, with a railroad at any time under Federal control; and (2) a sleeping car company whose system of transportation is under Federal control at the time Federal control terminates; but does not include a street or interurban electric railway not under Federal control at the time Federal control terminates, which has as its principal source of operating revenue urban, suburban, or interurban passenger traffic or sale of power, heat, and light, or both;

The term 'guaranty period' means the six months beginning March 1, 1920.

The term 'test period' means the three years ending June 30, 1917; and

The term 'railway operating income' and other references to accounts of carriers by railroad shall, in the case of a sleeping car company, be construed as indicating the appropriate corresponding accounts in the accounting system prescribed by the Commission.

(b) This section shall not be applicable to any carrier which does not on or before March 15, 1920, file with the Commission a written statement that it accepts all the provisions of this section.

(c) The United States hereby guarantees—

(1) With respect to any carrier with which a contract (exclusive of so-called cooperative contracts or waivers) has been made fixing the amount of just compensation under the Federal Control Act, that the railway operating income of

such carrier for the guaranty period as a whole shall not be less than one-half the amount named in such contract as annual compensation, or, where the contract fixed a lump sum as compensation for the whole period of Federal operation, that the railway operating income of such carrier for the guaranty period as a whole shall not be less than an amount which shall bear the same proportion to the lump sum so fixed as six months bears to the number of months during which such carrier was under Federal operation, including in both cases the increases in such compensation provided for in section 4 of the Federal Control Act;

(2) With respect to any carrier entitled to just compensation under the Federal Control Act, with which such a contract has not been made, that the railway operating income of such carrier for the guaranty period as a whole shall not be less than one-half of the annual amount estimated by the President as just compensation for such carrier under the Federal Control Act, including the increases in such compensation provided for in section 4 of the Federal Control Act. If any such carrier does not accept the President's estimate respecting its just compensation, and if in proceedings under section 3 of the Federal Control Act it is determined that a larger or smaller annual amount is due as just compensation, the guaranty under this paragraph shall be increased or decreased accordingly;

(3) With respect to any carrier, whether or not entitled to just compensation under the Federal Control Act, with which such a contract has not been made, and for which no estimate of just compensation is made by the President, and which for the test period as a whole sustained a deficit in railway operating income, the guaranty shall be a sum equal to (a) the amount by which any deficit in its railway operating income for the guaranty period as a whole exceeds one-half of its average annual deficit in railway operating income for the test period, plus (b) an amount equal to one-half the annual sum fixed by the President under section 4 of the Federal Control Act;

(4) With respect to any carrier not entitled to just compensation under the Federal Control Act, which for the test period as a whole had an average annual railway operating income, that the railway operating income of such carrier for the guaranty period as a whole shall not be less than one-half

the average annual railway operating income of such carrier during the test period.

(d) If for the guaranty period as a whole the railway operating income of any carrier entitled to a guaranty under paragraph (1), (2) or (4) of subdivision (c) is in excess of the minimum railway operating income guaranteed in such paragraph, such carrier shall forthwith pay the amount of such excess into the Treasury of the United States. If for the guaranty period as a whole the railway operating income of any carrier entitled to a guaranty under paragraph (3) of subdivision (c) is in excess of one-half of the annual sum fixed by the President with respect to such carrier under section 4 of the Federal Control Act, such carrier shall forthwith pay the amount of such excess into the Treasury of the United States. The amounts so paid into the Treasury of the United States shall be added to the funds made available under section 202 for the purposes indicated in such section. Notwithstanding the provisions of this subdivision, any carrier may retain out of any such excess any amount necessary to enable it to pay its fixed charges accruing during the guaranty period.

(e) For the purposes of this section railway operating income, or any deficit therein, for the test period shall be computed in the manner provided for in section 1 of the Federal Control Act.

(f) In computing railway operating income, or any deficit therein, for the guaranty period for the purposes of this section—

(1) Debits and credits arising from the accounts, called in the monthly reportly to the Commission equipment rents and joint facility rents, shall be included, but debits and credits arising from the operation of such street electric passenger railways, including railways commonly called interurbans, as are not under Federal control at the time of termination thereof, shall be excluded;

(2) Proper adjustments shall be made (a) in case any lines which were, during any portion of the period of Federal control, a part of the railroad or system of transportation of the carrier, and whose railway operating income was included in such income of the carrier for the test period, do not continue to be a part of such railroad or system of transporta-

tion during the entire guaranty period, and (b) in case of any lines acquired by, leased to, or consolidated with, the railroad or system of transportation of the carrier at any time since the end of the test period and prior to the expiration of the guaranty period, for which separate operating returns to the Commission are not made in respect to the entire portion of the guaranty period;

(3) There shall not be included in operating expenses, for maintenance of way and structures, or for maintenance of equipment, more than an amount fixed by the Commission. In fixing such amount the Commission shall so far as practicable apply the rule set forth in the proviso in paragraph (a) of section 5 of the "standard contract" between the United States and the carriers (whether or not such contract has been entered into with the carrier whose railway operating income is being computed);

(4) There shall not be included any taxes paid under Title I or II of the Revenue Act of 1917, or such portion of the taxes paid under Title II or III of the Revenue Act of 1918 as by the terms of such Act are to be treated as levied by an Act in amendment of Title I or II of the Revenue Act of 1917; and

(5) The Commission shall require the elimination and restatement of the operating expenses and revenues (other than for maintenance of way and structures, or maintenance of equipment) for the guaranty period, to the extent necessary to correct and exclude any disproportionate or unreasonable charge to such expenses or revenues for such period, or any charge to such expenses or revenues for such period which under a proper system of accounting is attributable to another period.

(g) The Commission shall, as soon as practicable after the expiration of the guaranty period, ascertain and certify to the Secretary of the Treasury the several amounts necessary to make good the foregoing guaranty to each carrier. The Secretary of the Treasury is hereby authorized and directed thereupon to draw warrants in favor of each such carrier upon the Treasury of the United States, for the amount shown in such certificate as necessary to make good such guaranty. An amount sufficient to pay such warrants is hereby appropriated out of any money in the Treasury not otherwise appropriated.

(h) Upon application of any carrier to the Commission, asking that during the guaranty period there may be advanced to it from time to time such sums, not in excess of the estimated amount necessary to make good the guaranty, as are necessary to enable it to meet its fixed charges, and operating expenses, the Commission may certify to the Secretary of the Treasury the amount of, and times at which, such advances, if any, shall be made. The Secretary of the Treasury, on receipt of such certificate, is authorized and directed to make the advances in the amounts and at the times specified in the certificate, upon the execution by the carrier of a contract, secured in such manner as the Secretary may determine, that upon final determination of the amount of the guaranty provided for by this section such carrier will repay to the United States any amounts which it has received from such advances in excess of the guaranty, with interest at the rate of 6 per centum per annum from the time such excess was paid. There is hereby appropriated, out of any money in the Treasury not otherwise appropriated, a sum sufficient to enable the Secretary of the Treasury to make the advances referred to in this subdivision."